Item	Present law
1. Underlying concept	Designed to allocate depreciation deductions over the period the asset is used in business so that deductions for the cost of an asset are matched with the income produced by the asset.
2. Eligible property	Assets used in a trade or business or for the production of income are depreciable if they are subject to wear and tear, decay or decline from natural causes, or obsolescence. Assets that do not decline on a predictable basis or that do not have a determinable useful life, such as land, goodwill, or stock, are not depreciable.
3. Useful lives (recovery periods) and methods	
a. Personal property	
Useful lives (recovery periods)	Under the ADR system, the Treasury, on the basis of actual industry experience, specifies a midpoint life for equipment used in most industries. Taxpayers may elect lives 20 percent longer or shorter than the midpoint life. ADR midpoint lives for equipment range from 2.5 years for certain special manufacturing tools to 50 years for certain public utility equipment. 1/
Method	New property - election to use straight-line up to the 200-percent declining balance, or sum of the years-digits (SYD) methods. Used property - election to use up to the 150-percent declining balance or straight-line methods.

1/ A cross-section of ADR lives is set forth in Table 1, p. 7.

Item	Present law	
3. Cont.		
b. Real property	IRS Guideline lives[2/]	Method
Factories, stores, warehouses	45-60 years	150-percent declining balance, if new, or straight-line.
Other nonresidential property	40-50 years	Same as above.
Low-income housing	40-45 years	New property.-Straight-line, 200-percent declining balance, or SYD. Used property- 125-percent declining balance (if property has a remaining useful life of 20 years) or straight-line.
Other residential property	40-45 years	Same as above.
c. Special rules	1. Taxpayer may use different lives for each separate component of a building, such as plumbing, wiring, etc. (component depreciation) or use a single life for the building and all components (composite depreciation).	
	2. ADR lives are prescribed for certain real property (e.g., farm buildings, theme park structures, and gas stations).	
4. Asset accounting	Item, group, or vintage closed accounts.[3/]	

[2/] Taxpayers often use shorter useful lives based on facts and circumstances. See Table 2 and 3, p. 7, for IRS guideline lives and average lives claimed by taxpayers.

[3/] Under a closed account system, assets ordinarily must be grouped according to the year property is placed in service.

Item	Present law
5. Salvage value	Property generally cannot be depreciated below estimated salvage value (salvage value limitation). For personal property, no salvage value limitation if salvage value is 10 percent or less.
6. Additional first-year depreciation	Optional bonus depreciation equal to 20 percent of property costs up to $10,000 per taxpayer (maximum allowable-$2,000).
7. Gain or loss upon disposition of assets	Deferral of gain or loss, in general, on retirements for causes such as wear and tear or obsolescence contemplated in determining useful life ("ordinary" or "normal" retirements). Current recognition of gain or loss on unanticipated dispositions, such as casualties or sale of a business ("extraordinary" or "abnormal" retirements).
8. Recapture of depreciation	
a. Personal property	Gain recognized on disposition is ordinary income rather than capital gain to the extent of prior depreciation taken (sec. 1245 recapture).
b. Real property	Gain recognized on disposition is ordinary income rather than capital gain only to the extent prior depreciation taken exceeds depreciation that would have been allowed if the straight-line method were used (sec. 1250 recapture).
9. Flexibility	a. Option to use useful lives 20 percent shorter or longer than ADR mid-point lives. b. Option to use straight-line or accelerated, where allowed. c. Required to deduct all depreciation allowable (i.e., no "banking"); net operating losses (NOL's) can be carried back 3 years and forward 7 years. d. Investment credit can be carried back 3 years and forward 7 years. e. Option to use an averaging convention to determine date of additions to and retirements from an account.

Item	Present law
10. Earnings and profits	Distributions to shareholders are taxable as dividends only to extent of earnings and profits. Depreciation deductions reduce earnings and profits. The amount of the reduction is based on straight-line depreciation over useful life (including lower limit of permitted ADR lives).
11. Depreciation of assets held outside U.S.	
a. Useful lives	No 20 percent variance from ADR midpoint life.
b. Methods	Accelerated methods generally allowed.
12. Add-on minimum tax and maximum tax	
a. Assets subject to application of add-on minimum tax	(1) Personal property leased by individuals, subchapter S corporations, and personal holding companies and (2) real property
b. Amount of tax preference item	Excess of allowable depreciation over amount allowable if the straight-line method were used over useful life (ADR midpoint only).
c. Tax preference offset for maximum tax	Amount of above tax preference item reduces amount eligible for 50 percent maximum tax.
13. Regular investment tax credit	
a. Amount of credit	Estimated useful life (years) — Credit (%) Less than 3 — 0 3-4 — 3-1/3 5-6 — 6-2/3 7 or more — 10
b. Used property limitation	Only $100,000 of used property eligible.
c. Recapture of credit	Credit recomputed on early disposition as if actual useful life had been used to determine amount of credit.
d. Carryover of credit	Investment credit can be carried back 3 years and forward 7 years.

14. At-risk Limitation	
a. Depreciation	For certain taxpayers, tax losses limited depending on the activity and the extent to which the taxpayer is at risk. 4/
b. Investment credit	No at-risk limitation.
15. Qualified progress expenditures	
a. Applicability	Investment tax credit (ITC) only.
b. Eligibility requirements	Property with 2-year normal construction period and 7-year useful life.
c. Self-constructed property	Progress expenditures allowed at time when amounts are properly chargeable to capital account.
d. Nonself-constructed property	Progress expenditures allowed when actual payment is made (payment rule) but only to the extent of progress in construction (progress rule). Amounts borrowed from the manufacturer or supplier not taken into account as progress expenditures (borrowing rule).
16. Rehabilitation expenditures	10-percent ITC for nonresidential rehabilitation.

4/ There is no at-risk limitation on the depreciation deduction itself. However, depreciation deductions, together with other deductions, may result in tax losses for an activity covered by the at-risk rule. Thus, there is an indirect limitation on the depreciation deduction.

Item	Present law
17. Lease financing	A transaction is characterized as a lease if -- 1. The owner's minimum at-risk investment throughout the lease term is 20 percent of cost; 2. The lessor has a positive cash flow and a profit from the lease independent of tax benefits; 3. The lease term does not include renewals or extensions at the option of the lessee at fair rental value; 4. The lessee does not have a right to purchase the property at less than fair market value; and 5. The lessee does not have an investment in the lease and does not lend any of the purchase costs to the owner.[5/]

5/ Rev. Procs. 75-21 and 75-28.

Table 1.—ADR Useful Lives of Various Assets

Description of assets in guideline class	Asset depreciation range (in years)		
	Lower limit	Asset guideline period	Upper limit
Certain short-lived assets:			
Manufacture of glass products—special tools	2.0	2.5	3.0
Manufacture of motor vehicles—Special tools	2.5	3.0	3.5
Breeding hogs	2.5	3.0	3.5
Certain intermediate-lived assets:			
Data handling equipment except computers	5.0	6.0	7.0
Assets used in drilling of oil and gas wells	5.0	6.0	7.0
Manufacture of apparel and other finished products	7.0	9.0	11.0
Certain long-lived assets:			
Vessels, barges, tugs, and similar water transportation equipment, except those used in marine contract construction	14.5	18.0	21.5
Telephone central office equipment	16.0	20.0	24.0
Railroad hydraulic electric generating equipment	40.0	50.0	60.0

Source: Revenue Procedure 77–10, 1977–1 C.B. 548, as amended.

Table 2.—Guideline Lives for Certain Buildings Under Revenue Procedure 62–21

Type of Building	Useful life (years)
Apartments	40
Banks	50
Dwellings	45
Factories	45
Garages	45
Grain Elevators	60
Hotels	40
Loft Buildings	50
Machine Shops	45
Office Buildings	45
Stores	50
Theaters	40
Warehouses	60

Table 3.—Comparison of Guideline Lives and Lives Claimed for Certain Building Types

(In years)

Building type	Guideline lives under Revenue Procedure 62–21	Average lives claimed by taxpayers (new buildings only)	Percentage of taxpayers claiming lives shorter than guideline lives
Retail (including shopping centers)	50	36	93
Warehouses	60	37	90
Factories	45	37	77
Office buildings	45	41	91
Banks	50	43	70
Apartments	40	32	78

Source: Office of Industrial Economics, Department of the Treasury, *Business Building Statistics* (GPO, Washington, 1975).